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Cautions against Using Statutory Demands Based on Adjudication Determinations

Introduction

In *Diamond Glass Enterprise Pte Ltd v Zhong Kai Construction Co Pte Ltd* [2021] SGCA 61, the Singapore Court of Appeal had the occasion of considering the interaction between the temporary finality of adjudication determinations under the statutory adjudication regime in the *Building and Construction Industry Security of Payment Act* (Cap 30B, 2006 Rev Ed) and the corporate insolvency regime. The case involved winding-up proceedings against the applicant company on the basis of an unsatisfied statutory demand for payment of the sum awarded under an adjudication determination. The Court granted a stay of winding-up proceedings as the applicant had shown the *prima facie* existence of justiciable cross-claims.

This is especially relevant in today's business climate with the expiry of the relief for financially distressed businesses under Part 3 of the COVID-19 (Temporary Measures) Act 2020 (No 14 of 2020).

Brief Facts

The case concerns a winding-up application made by Diamond Glass Enterprise Pte Ltd ("DG") as the creditor of Zhong Kai Construction Co Pte Ltd ("ZK"). DG obtained an adjudication determination ("AD") against ZK, entered judgment against ZK based on the AD, and then served a statutory demand on the adjudicated amount.

Despite these efforts, ZK did not make payment of the adjudicated amount, or commence proceedings to invalidate the AD.

Instead, ZK initiated two suits against DG, claiming liquidated damages and costs to complete the contract with DG. ZK relied on these as cross-claims against DG.

Contribution Note: This Client Update was written with contributions from Ching Meng Hang, Senior Associate, from Construction & Projects.



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Holding of the Court of Appeal

The Court recognised that, under SOPA section 21(1), adjudication determinations are temporarily final until reserved by the court or arbitral tribunal. Hence, it was open to DG to proceed with enforcement of the AD.

However, in winding-up proceedings, the Court recognised that a debtor is entitled to raise cross-claims against the creditor based on substantial grounds.

Hence, as a "*practical and workable solution to the apparent opposing considerations*" above, the Court applied the *prima facie* standard of review – the debtor may show that there was a *prima facie* existence of a justiciable cross-claim that is likely to equal or exceed the claim against the debtor.

On the facts, the Court held that ZK successfully established such *prima facie* cross-claims, and accordingly ordered that DG's winding-up application against ZK be stayed pending the determination of the suits. The Court also ordered that, as a condition to the stay, ZK pay the adjudicated amount into the Court.

Implications for the Industry

The Court of Appeal's decision raises implications for successful claimants in statutory adjudication.

A. Enforcement of adjudication determinations by statutory demand and winding-up

The service of statutory demands has been a common method to secure payment of adjudicated amounts backed by the threat of winding-up. Under section 125(2) of the Insolvency, Restructuring and Dissolution Act 2018 (No 40 of 2018), a company is deemed unable to pay its debt if it has for three weeks after the service of a statutory demand neglected to pay the creditor making the demand. Hence, a creditor may serve a statutory demand on a debtor and after the expiry of the three-week period proceed with a winding-up application against the company. Given the threat of a winding up, a debtor may then attempt to pay, or to secure or compound the debt.

However, the case significantly limits the utility of such an approach. This is because, when faced with a winding-up application, it is open to the debtors to raise cross-claims, whether such cross-claims have been the subject of the adjudication proceedings.

- (a) It appears that a debtor is now entitled to "reopen" matters that have been the subject of the adjudication determination, and to raise them as cross-claims against the creditor. On the facts, it appears that ZK had raised the issue of costs to complete in the adjudication. However, this

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did not appear to be an obstacle to ZK relying on the same issue as a cross-claim against DG. This significantly undercuts the temporary finality of an adjudication determination in winding-up proceedings.

- (b) Further, the debtor is also entitled to raise other matters that have not been the subject of the adjudication determination. On the facts, it appears that ZK had not raised the issue of liquidated damages in the adjudication, having failed to allege delays in its payment response. Again, this did not appear to be an obstacle to ZK relying on liquidated damages as a cross-claim against DG.
- (c) Relatedly, the debtor is also entitled to raise cross-claims on matters it would not have been entitled to raise in adjudication. In adjudication proceedings, SOPA imposes restrictions on the respondent's reliance on, for example, (i) damages, loss or expense that may be precluded under SOPA s 17(2A), or (ii) claims arising from a different contract between the same parties, as in *Civil Tech Pte Ltd v Hua Rong Engineering Pte Ltd* [2018] 1 SLR 584. No such restrictions apply in winding-up proceedings.

While it remains possible for the creditors to demonstrate that such cross-claims (i) are raised in abuse of the court's process merely to delay winding-up proceedings, or (ii) do not meet the *prima facie* standard of review, this would not be easy except in the clearest of cases.

Hence, the utility of statutory demands appears limited to situations where the debtors, "*despite raising such disputes or cross-claims, are hopelessly insolvent*".

Given the above, attempting to enforce adjudication determinations based on statutory demand would be an uphill task. It may be much more straightforward for a creditor to attempt enforcing the adjudication determination judgment using the remedies under SOPA, or writs of execution available under the Rules of Court. As the Court recognised, "*even if the winding-up application is stayed or dismissed, other avenues to obtain judgment debt still remain*".

- (a) Once a creditor obtains an adjudication determination, SOPA provides for the right of a creditor who is not paid the adjudicated amount to suspend work (SOPA section 26(1)(d)) or to take a lien on goods supplied (SOPA section 25(2)(d)).
- (b) Thereafter, the creditor may enforce the adjudication determination as a judgment and initiate execution proceedings, for instance, garnishee orders or writs of seizure and sale on the debtor's assets.

These constitute a more straightforward option to realise the fruits of adjudication proceedings, and accordingly present a more immediate need for the debtor to pay the adjudicated amount.

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B. Condition of stay

In the event that a winding-up application has been made based on an adjudication determination and may be subject to cross-claims, the Court's guidance on the conditions of staying such a winding-up application is also relevant.

The Court, in ordering ZK to pay the adjudicated amount into court as security, considered that had ZK applied to set aside the adjudication determination, ZK would have been required to make such payment into Court under SOPA section 27(6). Further, upon such payment, there would be no justification to presume that ZK was insolvent.

However, the Court also remarked that there may be situations where it would be unjust to order such payment into court pending litigation or arbitration, such as where *"the project is at the end or in the defects liability phase or has been terminated"*.

In such a situation, the creditor may consider availing itself to other remedies under SOPA and the Rules of Court as set out above. The creditor may also attempt to apply for security for costs in the litigation or arbitration proceedings on the grounds of impecuniosity, although the Court's observation above may be a potential factor making it more difficult to obtain such an order.

Ultimately, whether to order such payment into court is within the court's discretion.

Conclusion

The decision came at an opportune time for the industry, when it is expected that the number of disputes and corporate insolvency would increase significantly due to the continued impact of the COVID-19 pandemic.

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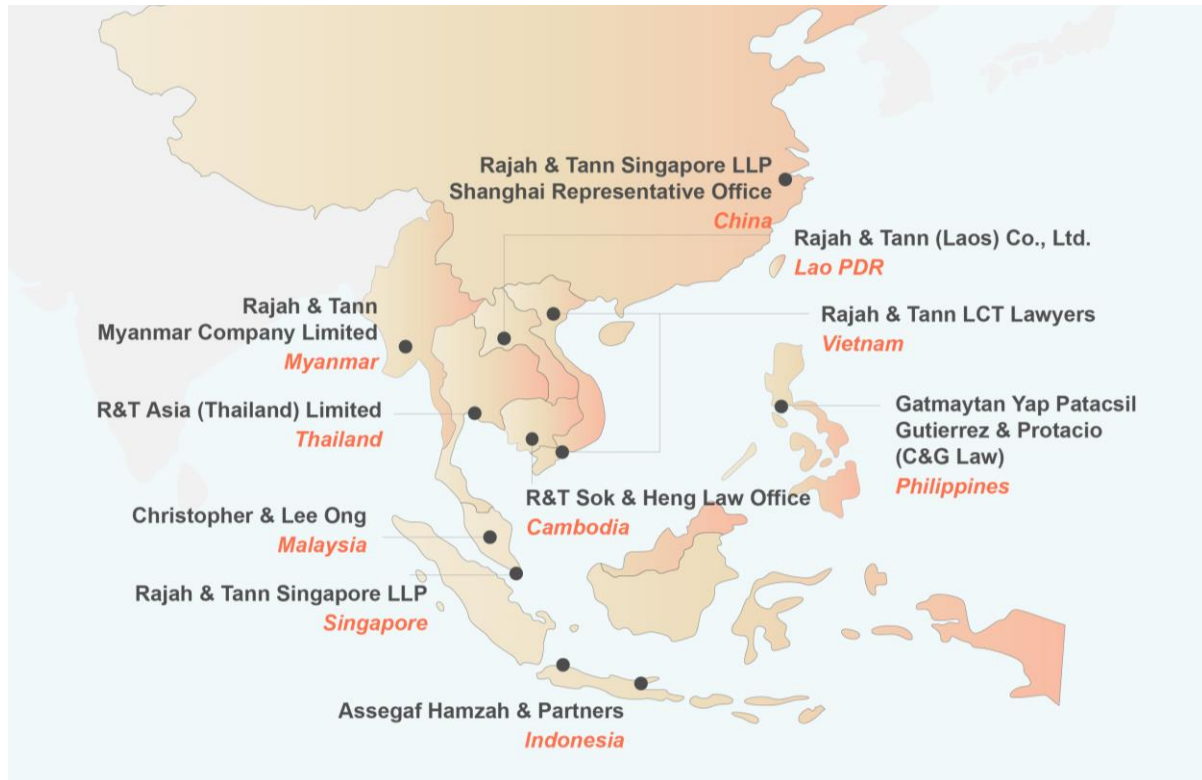
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